IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
(ALEXANDRIA DIVISION)

UNITED STATES OF AMERICA, *ex rel.* JON H. OBERG,	)	
Plaintiff,	)	
v.	)	CIVIL NO. 1:07-CV-960
NELNET, INC., PENNSYLVANIA HIGHER EDUCATION ASSISTANCE AGENCY, KENTUCKY HIGHER EDUCATION STUDENT LOAN CORPORATION, PANHANDLE PLAINS HIGHER EDUCATION AUTHORITY, SLM CORPORATION, SOUTHWEST STUDENT SERVICES CORPORATION, VERMONT STUDENT ASSISTANCE CORPORATION, EDUCATION LOANS INC/SD, BRAZOS HIGHER EDUCATION SERVICE CORPORATION, and ARKANSAS STUDENT LOAN AUTHORITY,	)	
Defendants.	)	

MEMORANDUM IN SUPPORT OF NELNET INC.'S MOTION TO DISMISS FOR FAILURE TO STATE A CAUSE OF ACTION AND FAILURE TO PLEAD FRAUD WITH PARTICULARITY

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Defendant Nelnet, Inc. ("Nelnet") respectfully submits this memorandum in support of its Motion to Dismiss Relator's First Amended Complaint (the "Complaint"), pursuant to Fed. R. Civ. P. 9(b) and 12(b)(6). The Complaint alleges that Nelnet and nine other defendants violated the False Claims Act ("FCA") in billing the United States Department of Education (the "Department") for certain statutory special allowance payments ("SAP") on student loans made under the Federal Family Education Loan Program ("FFELP").

As set forth below, the Complaint does not adequately allege scienter, a required element of a claim under the FCA, and thus Relator fails to properly allege that Nelnet knowingly presented any false or fraudulent claims for SAP to the Department. Instead, the allegations of the Complaint, at best, reflect a dispute concerning the proper interpretation of the Higher Education Act ("HEA") of 1965, as amended, and regulations issued under that Act governing the billing of SAP on certain types of loans. The Fourth Circuit has made clear that a good faith dispute on interpretation of a statutory provision does not constitute a violation of the FCA. *United States ex rel. Wilson v. Kellogg Brown & Root, Inc.*, 525 F.3d 370, 376-77 (4th Cir. 2008) ("*Wilson*"). Indeed, dismissal of the claims against Nelnet is particularly appropriate here, where the Department has explicitly acknowledged in a Settlement Agreement that Nelnet's actions were taken in good faith. Interpretation of the HEA and regulatory provisions concerning SAP is precisely at issue in this lawsuit. The Settlement Agreement is expressly referenced in the Complaint and thus is properly considered by this Court in ruling on Nelnet's Motion to Dismiss.[1]

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[1] *See SunTrust Bank v. Aetna Life Ins. Co.*, 251 F. Supp. 2d 1282, 1287 (E.D. Va. 2003) ("In evaluating a motion to dismiss pursuant to Federal Rule of Civil Procedure 12(b)(6), not only will the court consider the facts as set forth in the complaint, but the court will also consider the documents attached to the complaint . . . and matters of public record whose authenticity is unquestioned . . . . When a plaintiff fails to introduce a pertinent document as part of his

Moreover, the Complaint does not establish a plausible claim that Nelnet intentionally submitted false claims to the Government and should be dismissed under the standards established by the Supreme Court in *Ashcroft v. Iqbal,* 129 S. Ct. 1937, 1949-50 (2009). Finally, the Complaint groups the defendants together with broad brush allegations instead of specific allegations as to each individual defendant, and thus fails to allege fraud with particularity under Rule 9(b). For the foregoing reasons, as elaborated below, Nelnet respectfully requests that the Court dismiss Relator's claims in their entirety under Fed. R. Civ. P. 12(b)(6) and 9(b).

INTRODUCTION

This case concerns student loans made under the FFELP which are the subject of an extensive and detailed federal statutory and regulatory scheme established by Congress and the Department. *See* Title IV of the HEA, 20 U.S.C. § 1071 *et seq*; 34 C.F.R. pt. 682; (Compl. ¶ 2). Under the FFELP, the federal government provides lenders with incentives to invest their capital to make student loans, by, among other things, making subsidy payments known as SAP designed to guarantee lenders a minimum rate of return on such loans. (Compl. ¶ 2.)

The Relator, a former Department employee,[2] filed his original complaint under seal in September 21, 2007. The Government declined to intervene on August 24, 2009, and Relator filed the Complaint that same day. The Complaint asserts claims against ten different FFELP lenders. Nelnet has separately and concurrently with this motion filed a motion to sever the

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complaint, the defendant may attach the document to a motion to dismiss the complaint and the Court may consider the same without converting the motion to one for summary judgment.") (internal citations and quotations omitted); *Phillips v. Pitt County Mem'l Hosp.*, 572 F.3d 176, 180 (4th Cir. 2009); *Sec'y of State for Def. v. Trimble Navigation Ltd.*, 484 F.3d 700, 705 (4th Cir. 2007).

[2] The U.S. Department of Justice, in its "Notice of Election to Decline Intervention" filed with the Court herein, has reserved the right to challenge Relator's "personal profit" from this suit, as "it appears that some or all of the material facts and documents that serve to support the allegations in the complaint were gained by the Relator while he served as an employee of the United States."

claims asserted against it, and a motion to dismiss the claims for improper venue or, in the alternative, to transfer venue pursuant to 28 U.S.C. § 1404(a).

The Complaint focuses on defendants' billing of SAP on FFELP loans made or purchased with funds obtained by the holder from the issuance of tax-exempt obligations originally issued prior to October 1, 1993. These loans, called "9.5% loans" or "floor loans", are billed at half the normal SAP rate, but subject to a floor special allowance rate of 9.5%. 20 U.S.C. § 1087-1(b)(2)(B); (Compl. ¶¶ 3-6).

Relator alleges that defendants repeatedly and fraudulently submitted claims for 9.5% SAP on a form known as Lender's Interest and Special Allowance Request and Report ("LaRS/799"). (Compl. ¶¶ 57-61.) Relator alleges that defendants "repeatedly recycled (or reinvested) funds generated from their 9.5[%] [l]oans to make or purchase new 9.5[%] [l]oans", and sold existing 9.5% loans to other financing vehicles such as taxable bonds and considered the proceeds from those transactions to be loan pay-offs, the proceeds of which were used to make new 9.5% loans. (*Id.* ¶ 60.) Relator further alleges that the above process was "repeated over and over to improperly expand the pool of 9.5% loans." (*Id.*)

As explained below, these allegations are insufficient as a matter of law to establish a claim against Nelnet under the FCA.

ARGUMENT

I. Standard of Review

In FCA cases, fraud must be pleaded with particularity, as required by Fed. R. Civ. P. 9(b). Thus, the complaint must contain allegations setting forth "the time, place, and contents of the false representations, as well as the identity of the person making the misrepresentation and what he obtained thereby." *Harrison v. Westinghouse Savannah River Co.*, 176 F.3d 776, 783-

84 (4th Cir. 1999) ("*Harrison*") (quoting 5 Charles Alan Wright and Arthur R. Miller, Federal Practice and Procedure § 1297, at 590 (2d ed. 1990)); *Wilson*, 525 F.3d at 379 ("These facts are often 'referred to as the 'who, what, when, where, and how' of the alleged fraud.'").

In addition, Fed. R. Civ. P. 8(a)(2) requires that "a pleading that states a claim for relief must contain . . . a short and plain statement of the claim showing that the pleader is entitled to relief . . . ." While a complaint need not contain detailed factual allegations, the United States Supreme Court recently made clear that to survive a motion to dismiss, a complaint must contain sufficient factual information to "state a claim to relief that is plausible on its face." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007). *Twombly* further held that while it does not require "detailed factual allegations," Rule 8 does require more than labels and conclusions, and a "formulaic recitation of the elements of a cause of action will not do." *Id.* at 555 (internal citations omitted). Under *Twombly*, a complaint must contain some alleged facts that are "enough to raise a right to relief above the speculative level," and achieves facial plausibility when it contains sufficient factual allegations supporting the reasonable inference that the defendant is liable for the misconduct alleged. *Id.* at 555-56; *see also Boy Blue, Inc. v. Zomba Recording, LLC*, No. 3:09-CV-483-HEH, 2009 U.S. Dist. LEXIS 84988, *3 (E.D. Va. Sept. 16, 2009).

Further, in ruling on a motion to dismiss, the court must distinguish between factual allegations, which the Court must assume as true, and mere legal conclusions offered as factual assertions. *Iqbal*, 129 S. Ct. at 1949-50; *Feeley v. Total Realty Mgmt.*, No. 1:08cv1212 (GBL), 2009 WL 2902505, at *12 (E.D. Va. Aug. 28, 2009) (dismissing claims alleging conspiracy to commit fraud). In *Iqbal*, the Supreme Court said:

> To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to "state a claim to relief that is plausible on its face." A claim

> has facial plausibility when the Plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged. The plausibility standard is not akin to a "probability requirement," but it asks for more than a sheer possibility that a defendant has acted unlawfully. Where a complaint pleads facts that are "merely consistent with" a defendant's liability, it "stops short of the line between possibility and plausibility of 'entitlement to relief.'"

129 S. Ct. at 1949-50 (internal citations omitted).

II. The Complaint Fails to State A Claim Against Nelnet With Respect to the Requisite Element of Scienter.

A. *Scienter Is an Element that Must Be Established by Relator under the FCA.*

The courts have made it abundantly clear that not every regulatory violation translates into a false claim:

> It is not the case that any breach of contract, or violation of regulations or law, or receipt of money from the government where one is not entitled to receive the money, automatically gives rise to a claim under the FCA . . . . The FCA is far narrower.

United States ex rel. Hopper v. Anton, 91 F.3d 1261, 1265 (9th Cir. 1996). *See also United States ex rel. Lamers v. City of Green Bay,* 168 F.3d 1013, 1020 (7th Cir. 1999) (*"Lamers")* ("the FCA is not an appropriate vehicle for policing technical compliance with administrative regulations"); *United States ex rel. Englund v. Los Angeles County*, No. S-04-282 LKK/JFM, 2006 U.S. Dist. LEXIS 82034, at *34 (E.D. Cal. Oct. 31, 2006) ("It is well established that the FCA is not a vehicle for ensuring regulatory compliance. . . . [V]iolations of laws, rules, or regulations alone do not create a cause of action under the FCA." (internal citations and quotations omitted)). The FCA requires, as an express statutory element, that the Relator prove that Nelnet "knowingly" presented a false or fraudulent claim for payment or approval to the United States Government. 31 U.S.C. § 3729(a)(1). The FCA defines the terms "knowing" and "knowingly" to be where the defendant "(1) has actual knowledge of the information; (2) acts in

deliberate ignorance of the truth or falsity of the information; or (3) acts in reckless disregard of the truth or falsity of the information." 31 U.S.C. § 3729(b).

Courts have consistently emphasized that the scienter element is critical in establishing the fraud contemplated by the FCA. For example, the Fourth Circuit in *Wilson* stated the general rule that the FCA imposes liability only on one who knowingly presents a claim for payment to the United States government "with the requisite scienter." 525 F.3d. at 376. The court in *X Corp. v. Doe* explained that "[t]he heart of fraud [in the FCA] is an intentional misrepresentation. A violation of a regulatory provision, in the absence of a *knowingly* false or misleading misrepresentation, does not amount to fraud." 816 F. Supp. 1086, 1093 (E.D. Va. 1993). *See also Harrison*, 176 F.3d at 789 (holding that allegations of poor and inefficient management are not actionable under the FCA). In order to demonstrate that a claim for payment presented by a defendant is "knowingly" false under the FCA, the "claim must be a lie." *Hindo v. Univ. of Health Sciences,* 65 F.3d 608, 613 (7th Cir. 1995). *See also Wang v. FMC Corp.,* 975 F.2d 1413, 1421 (9th Cir. 1992) ("The phrase 'known to be false' in [the FCA] does not mean 'scientifically untrue'; it means 'a lie.'"). The lie must represent an objective falsehood. *Wilson*, 525 F.3d at 376. *See also Lamers,* 168 F.3d at 1018; *United States ex rel. DRC, Inc. v. Custer Battles, LLC*, 472 F. Supp. 2d 787, 797 (E.D. Va. 2007) ("*DRC, Inc.*").

B. *Disposing of Relator's Complaint as to Nelnet on the Scienter Issue Is Appropriate at the Motion to Dismiss Stage.*

In an FCA suit where the defendant relies upon its interpretation of a controlling law, regulation or contractual provision, it is well settled that the requisite scienter element is negated where the defendant presents a claim to the government based upon a position taken on a disputed legal question, or an unclear area of the law, even if defendant's position or interpretation ultimately does not prevail. Under those circumstances, where defendant's

interpretation is objectively reasonable, the defendant has not acted "in reckless disregard." 31 U.S.C. § 3729(b)(3). *See, e.g.*, *Wilson*, 525 F.3d at 377 ("[D]ifferences in interpretation growing out of a disputed legal question are . . . not false under the FCA." (quoting *Lamers*, 168 F.3d at 1018)); *DRC, Inc.*, 472 F. Supp. 2d at 797 n.15 ("[S]tatements as to conclusions about which reasonable minds may differ cannot be false." (citations omitted)). [3]

In *Wilson*, the Fourth Circuit affirmed the dismissal of an FCA claim under Fed. R. Civ. P. 12(b)(6) where the allegations contained in the complaint were premised, "not on an objective falsehood," but rather upon an interpretation of the controlling contractual provision. 525 F.3d at 377. The Fourth Circuit ultimately concluded that "differences in interpretation growing out of a disputed legal question" are not actionable, as an interpretation of a disputed law or contract provision cannot demonstrate an "objective falsehood." *Id.*[4] *See also X Corp.*, 816 F. Supp. at 1092 (expressing the general rule that "[t]he heart of fraud is an intentional misrepresentation," and basing its decision for the defendant in part on the fact that "[n]o one, including Doe [the attorney], had a clear understanding of what the [federal acquisition regulations] required in this context"); *Hagood v. Sonoma County Water Agency*, 81 F.3d 1465, 1479 (9th Cir. 1996) (ruling that "to take advantage of a disputed legal question, as may have happened here, is to be neither deliberately ignorant nor reckless disregardful . . . . At most, [the defendant] took advantage of a

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[3] *See also*, *United States v. Prabhu*, 442 F. Supp. 2d 1008, 1031 (D. Nev. 2006); *United States ex rel. Swafford v. Borgess Med. Ctr.*, 98 F. Supp. 2d 822, 832-33 (W.D. Mich. 2000), *aff'd,* 24 Fed. Appx. 491 (6th Cir. 2001); *United States ex rel. Bettis v. Odebrecht Contractors of Cal. Inc.*, 297 F. Supp. 2d 272, 291 (D.D.C. 2004), *aff'd,* 393 F.3d 1321 (D.C. Cir. 2005); *United States ex rel. Hochman v. Nackman*, 145 F.3d 1069, 1075-76 (9th Cir. 1998); *United States ex rel. K&R Ltd. v. Mass. Hous. Fin. Agency*, 456 F. Supp. 2d 46, 62 (D.D.C. 2006), *aff'd,* 530 F.3d 980 (D.C. Cir. 2008).

[4] It is a well established general proposition that the interpretation of a statute or regulation is a question of law. *Frahn v. United States*, 492 F.3d 258, 262 (4th Cir. 2007); *United States v. Boynton*, 63 F.3d 337, 342-44 (4th Cir. 1995); *United States v. UPS Customhouse Brokerage, Inc.*, 575 F.3d 1376 (Fed. Cir. 2009).

disputed legal issue. This, as we have previously held, is not enough." (internal citations and quotations omitted)); *Lamers*, 168 F.3d at 1018 (holding that "differences in interpretation growing out of a disputed legal question are similarly not false under the FCA").

Subsequent to the Fourth Circuit's affirmation of the 12(b)(6) dismissal in *Wilson*, the U.S. Supreme Court ruled that a defendant's reliance on an objectively reasonable interpretation of a legal obligation precludes a finding of "willfulness," irrespective of any evidence of the defendant's subjective intent. In the jointly decided *GEICO General Insurance Company v. Edo* and *Safeco Insurance Company v. Burr*, the Court held that "willfulness" as used in the Fair Credit Reporting Act (FCRA) means "reckless disregard." 551 U.S. 47 (2007). The scienter standards of the FCRA and the FCA are, therefore, identical. The *GEICO/Safeco* ruling found that the common law conceives of civil recklessness "as conduct violating an *objective* standard: action entailing 'an unjustifiably high risk of harm that is either known or so obvious that it should be known.'" *Id.* (citations omitted and emphasis added). By definition, a reasonable reading of the law cannot be reckless, and whether a defendant's interpretation of the law is reasonable is an objective consideration that a court may decide as a matter of law. The Court explicitly dismissed subjective bad faith of the defendant as having any bearing in the analysis of whether an interpretation of the law is reckless:

> Respondents-Plaintiffs argue that evidence of subjective bad faith must be taken into account in determining whether a company acted knowingly or recklessly . . . . To the extent that they argue that evidence of subjective bad faith can support a willfulness finding even when the company's reading of the statute is objectively reasonable, their argument is unsound. Where, as here, the statutory text and relevant court and agency guidance allow for more than one reasonable interpretation, it would defy history and current thinking to treat a defendant who merely adopts one such interpretation as a knowing or reckless violator. Congress could not have intended such a result for those who followed an interpretation that could reasonably have found support in the courts, whatever their subjective intent may have been.

Id. at 70 n.20.

The Court in *GEICO/Safeco* ultimately found that the lack of clarity in the controlling law, combined with the defendant's plausible interpretation of that law, was persuasive in determining that the interpretation, even though erroneous, was nonetheless reasonable; this determination foreclosed a finding of willfulness/recklessness as a matter of law. Thus, the Supreme Court essentially approved of the approach taken in *Wilson* and other cases under the FCA finding lack of scienter where the dispute involved an interpretation of law and the defendant's interpretation was plausible.

Under *GEICO/Safeco,* a court should dismiss an FCA suit if it finds that defendant's conduct is consistent with a reasonable interpretation of the law regardless of whatever allegations of subjective intent are pleaded. Multiple courts have now adopted the Supreme Court's *GEICO/Safeco* analysis in FCA suits. *See, e.g.*, *United States ex rel. K&R Ltd. v. Mass. Hous. Fin. Agency*, 530 F.3d 980, 983-84 (D.C. Cir. 2008); *United States ex rel. Hixson v. Health Mgmt. Sys., Inc.,* No. 4:07-cv-0465-JAJ, 2009 U.S. Dist. LEXIS 89768, at *40-42 (S.D. Iowa Sept. 21, 2009) (granting defendant's motion to dismiss based on the *Geico/Safeco* ruling and holding that "the lack of clarity regarding the proper interpretation of the regulations indicates that no basis exists for imposing FCA liability on Defendants, who merely adopted a reasonable interpretation of regulatory requirements. . . . Here, Defendants acted according to a plausible interpretation of the law that no court had ever contradicted."); *United States ex rel. Pritsker v. Sodexho, Inc.,* No. 03-6003, 2009 U.S. Dist. LEXIS 51469, at *54 (E.D. Pa. Mar. 6, 2009) (granting defendants' Rule 12(b)(6) motion to dismiss, based on *Geico/Safeco*). *See also* John T. Boese, Civil False Claims and Qui Tam Actions § 2.06(C), at 2-203-04 (2009-I Supp.) (3d ed. 2009) ("disputes involving ambiguous provisions should be capable of disposition . . . at

the motion to dismiss stage because the 'purely legal issue of reasonableness' may be evaluated by the . . . courts under the FCA's objective reckless disregard standard . . . .").

The case law discussed above, both before and after *GEICO/Safeco,* makes clear that if a legal dispute exists with respect to the laws or regulations controlling billings by a defendant in an FCA suit, the defendant's adoption of a position or interpretation in that dispute negates the element of scienter that the Relator must establish. Had this well settled rule not been adopted by the courts, every time a person presenting a claim to the federal government violated a regulation or breached a contractual term, it would trigger liability under the FCA. However, mechanisms are already in place to effectively handle regulatory violations and breaches of contract. The FCA and its heightened liability were intended only for those instances where the government establishes that the claim was *knowingly* false.

C. *The Complaint Should Be Dismissed Since Nelnet's Claims Were Based upon a Reasonable Interpretation of the 9.5% SAP Regulation.*

The Complaint in this case involves nothing more than a dispute over the correct interpretation of the controlling regulations governing SAP and should therefore be dismissed in accordance with *Wilson.* The Relator has alleged that in 2007 the Department took a legal position contrary to the positions of at least ten different student loan lenders, each of which have now been sued by the Relator. (Compl. at ¶ 71.) The Department, after paying the defendants' 9.5% SAP billings for many years, issued a new Dear Colleague Letter on January 23, 2007, in which it disputed those billings for the first time. (*Id.*) Thus a legal dispute or debate existed with respect to whether the defendants billed properly under laws and regulations existing at the relevant time period.

Nelnet's interpretation of the 9.5% SAP regulations can be seen in the May 29, 2003 letter that Nelnet submitted to the Department seeking guidance on its billing practices for the

9.5% SAP. A copy of the letter to the Department is attached hereto as Exhibit 1. (*See also* Compl. ¶ 76.) In this letter, Nelnet specifically advised the Department that it was seeking "to confirm the proper way to submit Lender's Request for Payment of Interest and Special Allowance (LaRS)." Nelnet proceeded to describe the procedures that it intended to utilize, including the possibility that the loans would be held in the tax-exempt Indenture for as little as one day.[5] Nelnet in essence set forth its interpretation of the regulations. In its response to Nelnet's inquiry, the Department raised no issues with the process outlined by Nelnet and continued to pay Nelnet's billings for 9.5% SAP thereafter. The fact that Relator now takes issue with that interpretation merely proves that this case involves a reasonable dispute over differing interpretations.

The allegations of the Complaint and the entire history of the 9.5% SAP provisions make clear that Nelnet's interpretation of the 9.5% SAP regulation was reasonable, plausible and undertaken in good faith. The Relator specifically acknowledges in the Complaint that Nelnet entered into a Settlement Agreement with the Department resolving the dispute as to the validity of the 9.5% SAP billings submitted by Nelnet to the Department. (Compl. at ¶ 67.) A copy of the Settlement Agreement, dated January 17, 2007, is attached hereto as Exhibit 2. As described below, the Settlement Agreement is striking evidence demonstrating Nelnet's good faith and reasonable interpretation of the 9.5% SAP regulation.

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[5] Relator apparently recognizes the fact that this letter presents an obstacle to his claim that Nelnet was submitting false claims. He alleges that the letter was calculated to mislead the Department, primarily because it did not accurately portray the purpose behind the practice. *See* (Compl. ¶ 76.) However, Relator fails to explain why the purpose of the practice is relevant or material to the inquiry. The reason for this is simple—the purpose is irrelevant to the determination of the legality of the practice. *See infra* section II(c), p. 24 of Nelnet's Memorandum, and cases cited therein, including *K&R Ltd.* and *Aflatooni.*

As the Complaint concedes, the Settlement Agreement was entered into by the Department following completion of the extensive audit of Nelnet by the Department's own OIG. (*Id.*) The Complaint, however, fails to mention critically important provisions contained in the Settlement Agreement.[6] First, the Department affirmatively permitted Nelnet to retain all previously billed and received 9.5% special allowance payments from the Department, and released Nelnet from any claim thereon. More important, however, are the provisions in the "Statement of Facts" of the Settlement Agreement to which the Department agreed. The Department acknowledged that Nelnet had billed the 9.5% SAP on certain loans through June of 2006, and agreed that "Nelnet considers it was authorized to do so." (Settlement Agreement, Ex. § I(E).) The Department further agreed that "[t]he OIG interpretation of the Higher Education Act and its implementing regulations differs from that of Nelnet." (*Id.* § I(F).) Most significant is the statement following a summary of the dispute between the Department and Nelnet over interpretation of applicable laws and regulations as they relate to the 9.5% SAP provisions:

> Nelnet and the Department agree that *bona fide, good faith disputes and controversies* exist between them concerning the matters described above.

(*Id.* § I(K) (emphasis added).)

In the terms of the Settlement Agreement, the Department agreed that "[t]o avoid further costs and risks of litigation . . . the parties have entered into this Agreement to resolve the issue

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[6] The Complaint noted that the settlement excluded actions under the FCA, (Compl. ¶ 67), although the allegations omitted the language in the Settlement Agreement explaining that "[t]he Department does not have authority to" settle actions under the FCA. (Settlement Agreement, Ex. 2 § II(K).) By statute, the United States Attorney General retains authority to settle all actions under the FCA. 31 U.S.C. § 3730(b)(1). All that this provision in the Settlement Agreement establishes is the unremarkable proposition that the Department lacks authority to settle an FCA case. *See Martin J. Simko Const., Inc. v. United States*, 852 F.2d 540 (Fed. Cir. 1988). However, that lack of authority does not mean that the Department, the entity charged with interpreting SAP provisions in the HEA, cannot assess whether a party under its jurisdiction has acted in good faith.

of Nelnet's past receipt of SAP payments under the 9.5 percent floor calculation on Project 950 loans and loans other than first-generation or second generation loans, as well as its rights with respect to future claims for SAP at the 9.5 percent floor calculation for such loans." (*Id.* § II(A).)

Thus the Department agreed and acknowledged in the Settlement Agreement with Nelnet that the dispute over the 9.5% billings was "bona fide" and in "good faith," and determined to settle that dispute to avoid the "risks" of litigation.[7] This is an extremely clear and express enunciation from the Department that Nelnet's interpretation of the 9.5% loan qualification provisions was made in good faith, without the required element of scienter under the FCA. The Settlement Agreement establishes that Nelnet acted under a reasonable good faith interpretation of the applicable law and regulations. It is difficult to imagine that the agency charged with administration and enforcement of the HEA and its implementing regulations could be the victim of fraud committed by a party having knowingly submitted a false claim, where that agency, with knowledge of the facts, acknowledges and agrees that the party submitting that claim did so (i) believing that it was authorized to do so, and (ii) in good faith and in the absence of any fraudulent intent.[8]

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[7] Over two centuries ago, the U.S. Supreme Court interpreted "bona fide" as signifying "a thing done really, with a good faith, without fraud, or deceit, or collusion, or trust." *Ware v. Hylton*, 3 U.S. 199, 241 (1796); *see also M. Lowenstein & Sons, Inc. v. British-American Mfg. Co.*, 7 F.2d 51, 53 (2d Cir. 1925). That interpretation has been incorporated into the standard legal definition of the word. *See* Black's Law Dictionary 168 (7th ed. 1999) (defining "bona fide" as "[m]ade in good faith; without fraud or deceit"). And courts, as a matter of law, have almost universally adopted this standard legal definition in cases interpreting the meaning of the term "bona fide." *See, e.g.*, *Electro Source, LLC v. Brandess-Kalt-Aetna Group, Inc.*, 458 F.3d 931, 936 n.3 (9th Cir. 2006); *Strangi v. Comm'r of Internal Revenue*, 417 F.3d 468, 479 (5th Cir. 2005); *Inge v. Rock Fin. Corp.*, 388 F.3d 930, 939 (6th Cir. 2004); *United States v. Schwimmer*, 924 F.2d 443, 448 (2d Cir. 1991); *Marroquin v. Canales*, 505 F. Supp. 2d 283 (D. Md. 2007); *Edwards v. McCormick*, 136 F. Supp. 2d 795, 801 n.8 (S.D. Ohio 2001).

[8] In revealing testimony before the House Committee on Education, the Secretary of Education responded to questions about the Settlement Agreement with Nelnet. The Secretary testified that she settled with Nelnet due to the significant risk of losing litigation:

A few days after the Department settled with Nelnet, the Department attached to its Dear Colleague Letter (FP-07-01) (referenced in the Complaint at paragraph 71 and available at) a more detailed letter that was sent to all lenders then claiming SAP at the 9.5% minimum rate. In the attached letter sent to all lenders then billing 9.5% SAP, the Department stated that "[t]he Department is committed to resolving without protracted dispute any potential objections both to the meaning and application of the statutory and regulatory requirements [with respect to 9.5% SAP billing] . . . . Therefore, the Department will not seek to recoup SAP already received in excess of that payable at the standard rate . . . for those lenders that [accept the Department's interpretation]." This position by the Department echoes the position taken by the Government in the *Wilson* case. In dismissing an FCA suit, the court emphasized that even though the relators claimed that the defendant did not properly perform the contract at issue, "the US government—the actual party to the contract—has not expressed dissatisfaction with" the defendant's performance of the contract. *Wilson*, 525 F.3d at 377. In *Lamers*, the relator in an FCA suit had alleged that the defendant had violated federal transit regulations in connection

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> I believed, and obviously anyone can second guess the legal settlement, that we [the Department] had significant exposure to this government and significant liability potential for not only this entity but potentially impacting others. And so that is why, I think, as a matter of prudence, I agreed to end, finally, this practice, settle that lawsuit for approximately $278 million, mitigating it against the nearly $1 billion of additional damage that might have been incurred had we lost that lawsuit. I worked with my inspector general to provide a methodology that would be sound and that could apply about legitimate reimbursements under that, and that is what we have done.
> * * *
> The reason that I settled this lawsuit, to get to your fundamental question, is because there was a risk of an additional nearly $900 million that this government was at risk of losing had we lost the lawsuit.

Transcript of Hearing Before the House Committee on Education and Labor, No. 110-32, at 30, 49 (May 10, 2007), attached hereto as Exhibit 3.

with its billings to the government. The court explained that the Federal Transit Administration (FTA) had decided to work with the defendant city to bring it into compliance with applicable federal regulations that the relator alleged had been violated in the defendant's billings. The court found as follows:

> Lamers [the relator], it seems, wants to use the FCA to preempt the FTA's discretionary decision not to pursue regulatory penalties against the City [for the regulatory violations]. But the FCA is not an appropriate vehicle for policing technical compliance with administrative regulations. The FCA is a fraud prevention statute; violations of the Federal Transit Act regulations are not fraud unless the violator knowingly lies to the government about them.

Lamers, 168 F.3d at 1020.

Indeed, for the Relator to advance this FCA suit following the Settlement Agreement and the Department's recognition of Nelnet's good faith interpretation improperly impinges upon the federal agency's discretionary authority. Courts have also held that "[t]o allow FCA suits to proceed where [the] government . . . may choose to waive administrative remedies, or impose a less drastic sanction than full denial of payment—would improperly permit qui tam [relators] to supplant the regulatory discretion granted to [the government]." *Englund*, 2006 U.S. Dist. LEXIS 82034, at *35. *See also United States ex rel. Siewick v. Jamieson Sci. & Eng'g*, 214 F.3d 1372, 1378 (D.C. Cir. 2000) ("[A] court that found contracts invalid in a qui tam action where the government has not joined the [relator] would have unilaterally divested the government of the opportunity to exercise the discretion . . . to accept or disaffirm the contract on the basis of complex variables reflecting the officials' views of the government's longterm interests."). Allowing the Relator to proceed here would supplant the regulatory discretion granted to the Government to the same extent as in *Siewick*.

Moreover, even apart from the Department's specific acknowledgement of Nelnet's good faith position in the Settlement Agreement, it is beyond question from the history of the

legislative and regulatory provisions governing 9.5% SAP, that Nelnet's interpretation of the governing SAP regulation was reasonable, plausible, and not frivolous. In 1980, Congress determined that lenders who financed their FFELP loans with tax-exempt bonds were enjoying an undue competitive advantage, and thus enacted legislation to reduce the SAP paid on loans financed by such tax-exempt bonds to one-half of the rate paid on loans financed by taxable bonds. At the same time, to protect lenders in the event interest rates fell, lenders were guaranteed a minimum 9.5% SAP on loans financed by tax-exempt obligations. 20 U.S.C. § 1087-1(b); (Compl. ¶ 3).

In 1993, Congress eliminated the reduced SAP (and the related 9.5% SAP floor) prospectively, but grandfathered the 9.5% SAP floor on loans already eligible for the 9.5% floor, as well as on loans made or purchased in the future with certain qualifying sources of funds. (Compl. ¶ 4.) After that change in law, federal regulations provided that several enumerated sources of funds could be used to continue to make or purchase loans that were subject to the 9.5% SAP floor. Two of the enumerated qualifying sources included "funds obtained by the holder from":

> (A) The proceeds of tax-exempt obligations originally issued prior to October 1, 1993;...[or]
>
> (D) The sale of a loan that was made or purchased with funds obtained by the holders from [pre October 1, 1993 tax-exempt obligations]...."

34 C.F.R. § 682.302(c)(3)(i)(A), (D); (Compl. ¶ 42).

Relator alleges that Nelnet sold "existing 9.5[% SAP] Loans [from Nelnet's 1985 tax-exempt financing] to other financing vehicles under the loan holder's control (such as a taxable bond). The lender would then...recycle those proceeds to make new 9.5[% SAP] Loans. This

process was repeated over and over to improperly expand the pool of 9.5[% SAP] Loans." (Compl. ¶ 60.) Nelnet was reasonable in its position that the loans purchased into the tax-exempt financing were purchased with qualifying sources of funds under the controlling regulations. First, Nelnet purchased new loans with the proceeds of the existing 9.5% SAP loans. As such, those proceeds used to purchase new loans were funds obtained by Nelnet from the proceeds of Nelnet's tax-exempt bond; thus Nelnet used a qualifying source of funds under 34 C.F.R. § 682.302(c)(3)(i)(A).

Relator's basic complaint about Nelnet's process to qualify loans for the 9.5% SAP appears to be that the process was "repeated over and over" to expand the portfolio of 9.5% SAP loans. (Compl. ¶ 60.) However, neither the HEA nor its implementing regulations defined the term "proceeds." In ordinary usage, the term "proceeds" encompasses proceeds of proceeds.[9] As loans were acquired with funds from "the proceeds of tax-exempt obligations" originally issued prior to October 1, 1993, it is reasonable to conclude that loans acquired by Nelnet with proceeds of proceeds of the tax-exempt obligations also were acquired with a qualifying source of funds under 34 C.F.R. § 682.302(c)(3)(i)(A). Nothing in the regulation requires that the proceeds be the "original" proceeds. The regulation expressly used the term "originally" when it intended to do so elsewhere in its reference to tax-exempt obligations "originally" issued prior to October 1, 1993. *Id.*

Alternatively, Nelnet used funds obtained from "the sale of a loan that was purchased" with funds obtained from a pre-October 1, 1993 tax-exempt bond as permitted in 34 C.F.R. § 682.302(c)(3)(i)(D). Nelnet "sold existing 9.5 Loans" and would then "recycle those proceeds to

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[9] *See* U.C.C. § 9-102, cmt 13.c. ("proceeds of proceeds are themselves proceeds"); *Bank of Cal. v. Thornton-Blue Pac., Inc.*, 62 Cal. Rptr. 2d 90, 94 n.4 (Cal. Ct. App. 1997) ("The term 'proceeds' includes proceeds of proceeds."); *In re Tri-State Equip., Inc.*, 792 F.2d 967, 970 (10th Cir. 1986) ("Proceeds will include proceeds of proceeds.").

make new 9.5 Loans." (Compl. ¶ 60.) As such, the use of funds obtained from the sale of existing 9.5% SAP loans would appear to fit squarely within the regulation controlling qualifying sources of funds. Relator's fundamental complaint with Nelnet's process, again, appears to be that Nelnet repeated the process "over and over" and increased the 9.5% SAP portfolio of loans. Nothing, however, in the regulation's text suggests that funds could only be obtained from the *initial* sale of a 9.5% SAP loan. The Department could have drafted the regulation (and interpreted it over many years) that way had it intended, but it did not.

The core of Relator's Complaint seems to be the allegation that Nelnet's process was designed to "expand the pool of 9.5[% SAP] Loans." (Compl. ¶ 60.) However, Relator concedes that the Department, through regulatory action (34 C.F.R. § 682.302(e)(2)) and sub-regulatory action (the 1996 Dear Colleague Letter cited in the Complaint) required a lender to bill at the reduced one half SAP rate (coupled with the 9.5% SAP floor) on loans transferred from tax-exempt to taxable financings, so long as that lender retained a legal interest in the loan and the original tax-exempt obligation had not been retired or defeased. (Compl. ¶ 5.) Thus when Nelnet "sold existing 9.5 Loans" to its taxable financing, as alleged in the Complaint at paragraph 60, it was reasonable for Nelnet to interpret the controlling regulations and guidance to allow for those loans to continue to be subject to the 9.5% SAP floor, in fact such an approach was required by the regulations and guidance. This naturally resulted in growth of Nelnet's 9.5% SAP portfolio.

Relator further asserts that by holding the loans in its 1985 tax-exempt bond for as little as one day, Nelnet did not satisfy the regulatory requirements to qualify for the 9.5% SAP. (Compl. ¶ 76.) However, nothing in the HEA or regulations requires a minimum amount of time

during which a loan must be financed by a tax-exempt obligation in order to qualify for the 9.5% SAP.

The House Budget Committee recognized the propriety of using proceeds from the sale of 9.5% SAP loans to qualify additional generations of 9.5% loans, stating that "[i]n 1996 the Clinton Administration issued another piece of administrative guidance that permitted loans to be transferred in and out of eligible bonds, allowing *still more loans* to become subject to the higher guaranteed rate of return." H.R. Rep. No. 109-276, at 218 (2005) (emphasis added).[10]

The reasonableness of Nelnet's interpretation of the law was further confirmed by the Taxpayer Teacher Protection Act of 2004, Pub. L. No. 108-409, 188 Stat. 2299, and in the Higher Education Reconciliation Act of 2005, Pub. L. No. 109-171, § 8001, 120 Stat. 4, 155, which were carefully crafted by Congress to proscribe future qualification of new loans for the 9.5% SAP (on a prospective basis only), and without impacting loans that had already been qualified. 20 U.S.C. § 1087-1. In both House and Senate debates, Congress discussed and rejected the possibility of retroactively shutting down the 9.5% SAP because it would affect lenders who relied upon these payments and who were told by the Federal Government years ago that this practice was legitimate. As a primary sponsor of the House bill put it, "the loan providers were told by the Clinton administration that it [Nelnet's process of qualifying loans for the 9.5% SAP] was perfectly legal and legitimate." 150 Cong. Rec. H8319 (Oct. 6, 2004). If the Relator's interpretation of the SAP regulation were correct, Congress would not have needed to amend the statute in 2004 or again in 2006 to end the practice prospectively. In *Pritsker*, , the court dismissed an FCA suit, based on the finding that the defendants' interpretation of the

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[10] Citation of legislative history is appropriate in a Rule 12(b)(6) motion. *See Anheuser Busch, Inc. v. Schmoke*, 63 F.3d 1305, 1312 (4th Cir. 1995), *rev'd on other grounds*, 517 U.S. 1206 (1996).

controlling regulations was reasonable and further explained as follows: "The reasonableness of [the defendants'] position is illustrated by [the agency's] change in [regulations], and OMB and OIG's differing opinions. Indeed, if the regulations clearly prohibited [defendants] from retaining rebates in the first place, there would have been no need to amend them . . . . " 2009 U.S. Dist. LEXIS 51469, at *53.

The Relator has gratuitously tossed into his Complaint lengthy allegations as to how Nelnet intended to profit from expanding its 9.5% SAP loan portfolio, as well as how Nelnet's profits increased, its stock price increased and the company paid its employees bonuses when it recognized the 9.5% SAP income. (Compl. ¶¶ 76, 79.) Such allegations are, however, irrelevant to the issue of scienter. An FCA defendant's motive to generate higher income has been held to have no bearing. *See K&R Ltd.*, 456 F. Supp. 2d at 62 ("The presence of a motive cannot substitute for evidence of knowledge and intent."); *United States v. Medica-Rents Co.*, 285 F. Supp. 2d 742, 772 (N.D. Tex. 2003).

United States ex rel. Aflatooni v. Kitsap Physicians Service, an FCA decision by the Ninth Circuit, highlights why Relator's claims involving Nelnet's subjective intent are wholly irrelevant to determination of this motion. 314 F.3d 995 (9th Cir. 2002). In *Aflatooni,* the court granted summary judgment in favor of the defendant in an FCA suit alleging false Medicare billings. The court noted that the Relator in that case had alleged a "scheme" in the billings intended to defraud the government, and that the individual physician involved in those billings "was 'greedy,' implying an improper motive...." *Id.* at 1002. The court rejected such allegations as "speculative suppositions" and explained that "[t]he False Claims Act . . . focuses on the submission of a claim, and does not concern itself with whether or to what extent there exists a menacing underlying scheme." *Id.*

In short, the Settlement Agreement, Nelnet's correspondence to the Department, and the entire history of Congressional and Department of Education actions relating to the 9.5% SAP regulation demonstrate that: (i) legal disputes existed between Nelnet and the Department over the precise issue the Relator has raised in this current action, i.e. interpretation of the SAP regulation which, in turn, controls the validity of Nelnet's methodology for qualifying student loans for SAP at the 9.5% rate; and (ii) Nelnet's interpretation of the applicable regulation was reasonable and taken in good faith. Accordingly, the Complaint should be dismissed because Nelnet did not knowingly submit any false claims for payment.

III. The Complaint Fails to Allege Fraud with Particularity.

The allegations in the Complaint also fail to adequately allege fraud with the degree of particularity required by Fed. R. Civ. P. 9(b).

Relator makes only general allegations about the alleged false representations without any reference to a specific defendant. Instead, the allegations are generic and conclusory, and completely lack the particularity required by Rule 9(b). Moreover, Relator claims that a variety of schemes and unlawful techniques were utilized by defendants who then made untenable self-serving interpretations to justify their actions:

--Defendants designed and implemented **a number of these unlawful schemes** for inflating 9.5 SAP claims, for example by repeatedly exchanging existing 9.5 loans for loans supported by taxable bonds, and then claiming that all such portfolios were 9.5% eligible. (Compl. ¶ 9.)

--Defendants used **various unlawful** techniques to expand their holdings of these lucrative loans. (*Id.* ¶ 10.)

--The schemes implemented by the Defendants to increase their 9.5 SAP loan portfolios necessarily rely...on **untenable, self-serving interpretations** of the relevant statute and regulations...that clearly defied the intent of the Congress. (*Id.* ¶ 11.)

--Defendants "employed **many methods** to increase their 9.5 Loan portfolios." Relator cites a single example of a method allegedly used by defendants. (*Id.* ¶ 60.)

There are several things that are readily apparent about the nature of these allegations. First, there are absolutely no details provided. Ten entirely different and unrelated companies are lumped together in the definition of "defendants." No details are provided about the time that the alleged misrepresentations were made by any of the ten companies, the place where they were made or who at any particular company made them. Indeed, in paragraph 60 of the Complaint, Relator alleges that the defendants employed many methods as part of their schemes and then details one such method. No attempt is then made to tie any particular defendant to any particular scheme or technique. As Judge Lee of this District held in *Feeley v. Total Realty Management,* dismissal is appropriate under Rule 9(b) where, as here, the complaint groups lenders together with broad brush allegations instead of making specific factual allegations against individual defendants. 2009 WL 2902505, at *2.

The only details provided by Relator about Nelnet's actions are in paragraphs 53, 66-67, 74-80 of the Complaint, and in these paragraphs, Relator does not provide any details of Nelnet's supposed scheme or technique. Relator merely alleges that Nelnet increased its 9.5% loans from $393 million in 2001 to $3.3 billion in 2004. No details at all are alleged as to how Nelnet accomplished this, when it occurred, or who was involved. Instead, Relator includes a number of allegations about the OIG's audit of Nelnet, Nelnet's attempts to communicate with the Department about its interpretation of the law governing these loans, Nelnet's decision to defer

recognizing the income from its billing for the 9.5% SAP, and Nelnet's ultimate recognition of the income. These latter allegations, however, do not supply the details required by Rule 9(b). Absent these details, the Complaint fails to satisfy the requirement of Rule 9(b) and it must be dismissed.

CONCLUSION

For the foregoing reasons Nelnet's motion to dismiss the First Amended Complaint should be granted for failure to state a claim upon which relief may be granted pursuant to Fed. R. Civ. P. 12(b)(6) and for failure to plead fraud with particularity pursuant to Fed. R. Civ. P. 9(b).

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Respectfully submitted,

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